SECTION 5

Financing Guidelines

Capital projects may be financed by a variety of methods ranging from cash to various forms of long-term debt. The most common financing alternatives and their distinguishing characteristics are described below. Each of these methods is more appropriate for some projects and less appropriate for others. Questions concerning the selection of financing options by the requesting agency, or about a specific financing proposal, should be referred to your OFM operating or capital budget analyst.

The use of debt financing allows the state to undertake the development or acquisition of capital assets not affordable within current state revenue. In this way, the state can realize the benefits of these assets while spreading the cost over a number of years. Debt financing represents the irrevocable commitment of future dollars and therefore must be evaluated in relationship to the long-term benefits it provides.

Agency needs for new capital assets, as well as preservation and renewal of existing state assets, will always far exceed available resources to pay for them. Projects financed with bond funds or other alternative long-term financing should be carefully chosen to reflect the highest priority capital needs for Washington State. The following OFM guidelines define when it is appropriate to use long-term financing to fund capital improvement projects and related costs and what form of financing is appropriate to the different types of projects.

5.1 Methods of Financing

- **General obligation bonds** are the traditional form of government debt financing for major construction projects. The state pledges full faith and credit and taxing power to pay principal and interest. The term of the bond is usually 25 years. The interest paid to investors is exempt from federal income tax and the rates are typically 2 percent below taxable bonds. General obligation bonds are subject to the 7 percent state debt limit. Legislation authorizing general obligation bonds requires a 60 percent vote by the Legislature.

- **Reimbursable bonds** are a form of general obligation bonds. The difference is the source of payment. Reimbursable bonds are paid from sources other than the general fund. In 1993, reimbursable bonds paid from sources within the state treasury were included under the debt limit and replaced revenue bonds.

- **Certificates of participation** (COP) are a form of debt financing contract with individual investors. COPs are sold in the public securities market and the interest earnings are tax-exempt. Debt service payments are made from operating budgets.

- **Lease purchase and lease development** cause a building to be built or substantially remodeled to state specifications by a private developer. In both cases, the developer finances the project and recovers the cost through lease payments. At the end of the lease period, the state may exercise the option to purchase at a predetermined price. There is no tax exemption for the developer and market interest rates prevail.

- **Long-term lease –** The standard lease term employed by the state is five years; however, if an agency has a consistent and stable presence in the location **AND** there is a demonstrated economic advantage to the state, a lease up to 10 years may be negotiated, and approved by GA. A long-term lease of up to 20 years can be negotiated by GA and must be approved by OFM. Long-term leases are not considered to be a debt of the state. Lease payments are made from agency operating budgets.

5.2 Allowable uses of Long-Term Financing

Acquisition - land and buildings

Expenditures for the acquisition of real property whether obtained by purchase or by condemnation under the applicable eminent domain laws of the state of Washington, include expenses directly and necessarily related to such purchase or condemnation. Acquisition expenditures may include the cost of existing structures improving the real property such as buildings, structures, facilities, roads, parking areas, and bridges. Financed land costs include the following: land and improvement costs, appraisal fees, title opinions, surveying fees, real estate fees, title transfer taxes, easements of record with an extended term, condemnation costs and related legal expenses.

Land purchases should be consistent with agency master plans and reflect actions taken to meet growth needs in the long-term. Financed land purchases for the purpose of investment or land banking should be avoided.

Consultant services - predesign and design

These are expenditures related to architectural/engineering planning and design required for developing and implementing a specific capital improvement project. They can include preliminary technical studies developed from program statements that reflect the functional characteristics and architectural requirements of a financed capital improvement project (predesign); costs for schematic design and design development; and completion of construction documents and detailed working drawings required for bidding and construction. Also included are costs for "extra and other services," and reimbursable expenses provided within an executed contract for professional and technical services (see Section 4). Fees for construction management and observation are also financed as part of the project.

Permit services

Fees for services for environmental or other construction permits required for developing and implementing a specific capital improvement project may be financed as part of the project.

Planning documents not appropriate for bond financing

Expenditures for general long-range development plans, master plans, historical or archeological research, feasibility studies, statements, energy audits or other expenditures similar in character are *not* financed from bonds or other long-term financing. These costs should be contained in the agency's operating budget.

Construction

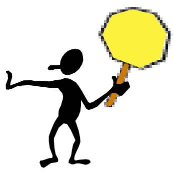
Site work – Site improvement expenditures include costs related to a financed capital improvement project including demolition, rough and final grading of a site, and the construction or replacement of sidewalks, road and driveway pavement surfaces, bridges, ramps, curbs, overpasses, underpasses, pedestrian bridges and tunnels, surface parking areas, campground development, building terraces, retaining walls, exterior lighting, and seeding or sodding for erosion control. Landscaping costs are financed only if included in a larger financed capital project. Site improvement projects not part of a larger capital project may be financed if the structure or improvement provided is permanent and meets all other tests and requirements of these guidelines. Demolition of buildings, structures, removal of trees and plant material, grading, rerouting utilities, and erosion control are financed when they precede a financed project to be undertaken on the same site. Clearing of land or demolition of vacant buildings is usually financed only in preparation for a financed construction project.

Financed road work may include construction of a new road or parking lot, extension of a road or parking lot, replacement, reconstruction, or upgrading a road or parking lot to a significantly more permanent surface. Examples include upgrading from gravel to oil and chip, oil and chip to asphalt, or asphalt to concrete. The financed road project includes all necessary signing, landscaping, erosion control, drainage, lighting, bridges, safety, and control structures. Repairs or resurfacing of existing roads to temporarily extend useful life are not financed.

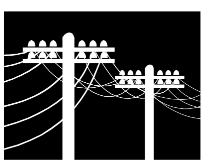
Examples of work financed through capital appropriations include the following:

- Purchase of existing facilities and tenant improvements.
- Reconstruction of an existing building or structure, which may include demolition, as well as installation of new structural or interior walls, floors, ceilings, utilities, interior finishes, furnishings, and equipment.
- Exterior work, including exterior surface, structural or foundation work necessary to extend the useful life of the structure.
- Roof work that removes all or major portions of a roofing system down to the decking and replacement with a new system. Replacement of insulation, decking, and other necessary structural work may be part of a financed roof replacement project. Included in a financed project may be stone or metal work and other work necessary to direct and control water drainage and ice formation. Non-financed roof repairs include; patching, replacing shingles, spot treatment with tar or other roof materials, adding gravel or other materials, or other repairs. Replacing gutters, downspouts, fascia and other work is not financed as a project but may be included as part of a larger financed roof replacement project.
- Interior work generally involves the following elements of work: demolition, moving walls, new carpet or floor surfaces, new finishes, replacing electrical and plumbing facilities, changes to the heating or cooling system, and installation of new fixed or moveable equipment.

Facilities preservation – Expenditures for the reconstruction or preservation improvement of existing buildings, or structures are a financed expense. This category includes site developments necessarily required or related to the preparation of a site for reconstruction purposes; and required built-in, special-purpose, or other fixed equipment where such equipment is permanently affixed or connected to real property in such a manner that removal would cause consequent damage to the real property to which it is affixed. Also included in this category are expenditures for the installation or replacement of water control structures such as dams, culverts, aqueducts, drainage systems, locks, spillways, reservoirs, and channel improvements. However, normally recurring expenses associated with water control structure improvements are not financed, unless part of a larger financed project.



Safety and codes – The justification or need for such work determines program and budget priority but does not affect the source of funds to pay for the work. The criteria in these guidelines for interior and utility work will determine whether the proposed safety or code project is financed. Examples of non-financed work, unless included in a larger financed remodeling or reconstruction project, include: installation of fire alarms, smoke detectors, or automatic door closers.



Utilities – Financed utility costs include expenditures for the acquisition, construction, replacement, modification or extension of utility systems including: construction or replacement of utility lines between buildings, replacement or installation of utilities to off-site supply systems, replacement of complete boiler or central air conditioning or ventilation systems. Financed utility improvements include:

- Provisions for potable water, high temperature water for sanitary or other related purposes, domestic hot or chilled water.
- Systems and associated components for disbursing or providing electricity or telecommunications service, including underground or overhead distribution cables for television, computers, or other modes of communication.

- Steam and condensate returns.
- Storm and sanitary sewers.
- Fire hydrants and stand pipes.
- Central fire and security alert systems.
- Lighting systems.
- Tap-ons or extensions related to existing utility systems.
- Automated temperature or environmental control systems, and air or water pollution control systems.
- Provisions for the disposal of contaminated, radioactive, hazardous or surgical waste.
- Solar heating or other approved energy systems as part of a financed construction or reconstruction project.
- Sewage and water treatment facilities, equipment and related systems.
- Earth moving to create artificial lakes or reservoirs for utility or related purposes.
- Restoration of natural and manmade features of the site.
- Trenches or ditches dug for the purpose of laying tile or providing other means to remove excessive rainfall and prevent erosion.

Non-financed utility repairs generally include minor replacement of corroded or leaking pipes inside a facility, replacement of unsafe or undersized wiring, repairs to stop leaks or replace radiators, replacing heating or cooling coils, replacing fans or motors, retubing boilers, adding controls or valves for energy conservation, replacement of thermostats or timers.

Equipment

Durable moveable equipment is the initial moveable equipment, other than built-in equipment, which is necessary and appropriate for the functioning of a particular facility for its specific purpose and which will be used solely or primarily in the rooms or areas covered in the subject project. Such equipment is defined as manufactured items which have an extended useful life, are not affixed to a building and are capable of being moved or relocated from room to room or building to building, are not consumed in use, and have an identity and function which will not be lost through incorporation into a more complex unit.

Durable moveable equipment and equipment affixed or built into the building or structure is considered fixed equipment and may be a financed expense.

The following items may be financed when such items are part of a larger financed project:

- Office equipment and furniture.
- Books, maps and other library materials.
- Personal computers and network systems, including related electronic hardware when part of a financed new construction or major programmatic remodeling project.
- Machinery, implements, and major tools.
- Scientific instruments and apparatus with the exception of those items which are subject to a short useful life, i.e., glassware, tubing, crockery, light bulbs, etc. These items are more correctly defined as commodities. (See below.)
- Items of equipment purchased in quantity and have a significant useful life of a minimum of 13 years. These items should be identifiable for inventory control purposes.

Transportation costs and installation costs incurred with an outside source will be considered as part of the equipment costs for items funded by bonds after appropriate review by OFM.

Non-financed equipment include:

- Commodities such as glassware, crockery, light bulbs, and office supplies.
- Spare and replacement parts.
- Consumable items such as paper, pens and chemistry supplies.

Other costs

Relocation costs are payments made to owners or occupants of property that the state is acquiring. These costs may be financed when paid pursuant to federal or state statutes. The cost of moving furniture, equipment and supplies between facilities for state facilities are operating costs and not included in capital projects.

Non-financed expenses

The following are operating or other types of expenditures that are specifically **NOT** financed in capital projects:

- The cost of moving furniture, equipment, and supplies between facilities should not be included in capital projects.
- Projects (appropriation titles) which cost less than $25,000 or which have an estimated useful life of less than 13 years.
- Ordinary maintenance such as: patching, painting, caulking, weatherproofing, insulating, adding storm windows, replacing doors, repairing vandalism or cleaning. An aggregation of ordinary maintenance does not create a financed capital project. Work undertaken as a result of deferred maintenance likewise does not normally make the project financed. Elements of work that are not financed if considered separately may be included in a larger financed project.
- Lease payments for rental of equipment or facilities.
- Costs for archeological digs, research, or exploration.
- Expenditures to acquire or construct temporary facilities or for facilities where abandonment or replacement is imminent. This does not include temporary facilities required by a contractor during construction such as a "job shack."
- Separate purchases of sand, gravel, rock, asphalt or concrete in limited quantities, ordinary hardware items, and temporary fencing.
- Spare or replacement parts and equipment, hand tools, SCUBA equipment, decorative models, plaques, commemorative memorabilia, supplies or other commodities.
- Purchase of automobiles, trucks, farm or construction equipment, boats, tractors, lawn mowers, fire engines, trailer mounted electrical generators, airplanes, helicopters and related items.
- Livestock or laboratory animals.

- Unpredictable or unusual legal expenses (other than those associated with land acquisition) which are not ordinarily provided within the budget for a capital project.

- Parking costs during construction.

- Agency expenses for capital budgeting, planning or other costs not directly related to the completion of a financed project.